

April 21, 2017

EDWARD J. EMMONS, CLERK
U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

Signed and Filed: April 20, 2017



Dennis Montali

DENNIS MONTALI
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA

In re) Bankruptcy Case
BLUE EARTH, INC.,) No. 16-30296 DM
) Chapter 11
Debtor.)

**MEMORANDUM DECISION REGARDING DEBTOR'S OBJECTION TO CLAIM NO. 105
FILED BY ROBERT C. FLOREK AND ASSIGNED TO TERESA JEAN MOORE**

I. INTRODUCTION

At a hearing on April 7, 2017, the court took under advisement the objection of Blue Earth, Inc. ("Debtor") to proof of claim number 105 ("Claim No. 105") filed by Robert C. Florek ("Florek") and assigned to Teresa J. Moore ("Moore"). For the reasons set forth below, the court will sustain the objection.

II. DISCUSSION¹

On August 1, 2016, Robert C. Florek ("Florek") filed a proof of claim ("Claim No. 105") in the amount of \$997,123.88. In response to Question 8 on the claim form ("What is the basis of the claim?"), Florek responded: "Millennium Power Solutions (MPS)

¹The relevant facts upon which the court reaches its conclusions are not in dispute.

1 Founding Subscriber." (Dkt. No. 330 at pg. 34). In particular,
2 as Florek stated in subsequent filings with the court, his claim
3 arose from a purchase for \$100,000 of 533,333 shares of Millennium
4 Power Solutions, LLC Class B Units, estimated to be a 5% ownership
5 interest in Millennium Power Solutions, LLC ("MPS"). (Dkt. No.
6 362 at pg. 2). He purchased the units pursuant to a subscription
7 agreement ("Subscription Agreement") dated May 1, 2012. (*Id.*;
8 Dkt. No. 363 at pg. 14).

9 On October 26, 2016, Blue Earth, Inc. ("Debtor") filed a
10 Fifth Omnibus Claim Objection (No Liability Claims) that included
11 an objection to Claim No. 105. (Dkt. No. 330). Florek filed an
12 opposition and declaration on December 2, 2016. (Dkt. Nos. 362 and
13 363).

14 On December 6, 2016, Florek executed a "Transfer of Claim
15 Other Than For Security" assigning his claim to Teresa J. Moore
16 ("Moore"). (Dkt. No. 429, Exh. 1). Three days later, Florek and
17 Moore executed a "Evidence of Transfer of Claim." (Dkt. No. 432
18 at p. 17). For purposes of this memorandum decision only, the
19 court will treat the transfer of Claim No. 105 to Moore as timely
20 and valid, without reaching the issue of whether the assignment
21 was time-barred pursuant to terms of the Debtor's confirmed plan
22 of reorganization.

23 On February 17, 2017, Debtor filed an omnibus reply (Dkt. No.
24 402) that included a response to Florek's opposition. Debtor
25 noted that Claim No. 105 was based on the purchase of stock in
26 another entity (MPS) and that Debtor was not a party to the
27 relevant Subscription Agreement. Debtor also observed that even
28 if it had been a party to the Subscription Agreement, the claim

1 sought damages arising from the purchase of stock and thus would
2 be subordinated to general unsecured creditors under 11 U.S.C. §
3 510(b).

4 The court held a hearing on the claim objection on February
5 24, 2017. Moore appeared and stated that she was the assignee of
6 the claim. The court continued the hearing to April 7, 2017, and
7 directed Moore to file a statement regarding the claim assignment
8 and her standing as an assignee. Moore did so on March 30, 2017
9 (Dkt. No. 428).

10 At the April 7 hearing, the court heard arguments regarding
11 Claim No. 105 and took the matter under submission. On April 10,
12 2017, Moore filed a motion to allow the assignment of Claim No.
13 105, to allow discovery and to allow opposition to the objection.
14 (Dkt. No. 432). Moore contended that she thought that the court
15 would limit the April 7 hearing to issues regarding the
16 "distribution record date" and the assignment of the claim to her,
17 even though the claim objection and reply clearly focused on two
18 grounds: (1) Florek purchased stock from an entity other than
19 Debtor and thus Debtor is not liable for damages arising from the
20 purchase of that stock, and (2) even if Debtor had been a party to
21 the underlying Subscription Agreement, any claims for damages
22 arising from the purchase of stock are subordinated to those of
23 general unsecured creditors pursuant to section 510(b).

24 While the court sympathizes with Moore's family difficulties,
25 it is denying her request for further time to respond as any such
26 response is unnecessary and would be futile. As a matter of law
27 and undisputed fact, the claim is not allowable.

28 First, the transaction upon which Florek bases his claim did

1 not involve Debtor. In 2012, Florek entered into a stock
2 Subscription Agreement with MPS for the purchase of five percent
3 ownership in MPS. See Declaration of Florek at Dkt. No. 363,
4 paragraphs 4, 9, 10 and Exhibits 3 and 4. His own opposition
5 concedes that his claim is based on "his 5% ownership interest in
6 the MPS by acquisition" and contends that the assets of MPS
7 (subsequently acquired in 2013 by Debtor's wholly-owned
8 subsidiary) secure that 5% interest. See Florek's Opposition at
9 Dkt. No. 362 at 2:14-18. Thus the liability he asserts against
10 Debtor arises from his acquisition of an equity interest from MPS,
11 not Debtor.

12 More importantly, even if Debtor had been a party to the
13 underlying subscription agreement, Florek's claim would be
14 subordinated to those of general unsecured creditors and thus
15 entitled to no distribution under the confirmed plan. Section
16 510(b) provides:

17
18 (b) For the purpose of distribution under this title, a
19 *claim arising from rescission of a purchase or sale of a*
20 *security of the debtor or of an affiliate of the debtor,*
21 *for damages arising from the purchase or sale of such a*
22 *security, or for reimbursement or contribution allowed*
under section 502 on account of such a claim, shall be
subordinated to all claims or interests that are senior
to or equal the claim or interest represented by such
security, except that if such security is common stock,
such claim has the same priority as common stock.

23 11 U.S.C. § 510(b) (emphasis added).

24 As the Ninth Circuit has recognized, section 510(b) "serves
25 to effectuate one of the general principles of corporate and
26 bankruptcy law: that creditors are entitled to be paid ahead of
27 shareholders in the distribution of corporate assets." *In re*
28 *American Wagering, Inc.*, 493 F.3d 1067, 1071-72 (9th Cir. 2007).

1 The principles behind corporate and bankruptcy laws
2 generally do not favor shifting the risk of loss from
3 shareholders to creditors, even if the shareholders are
4 blameless. One of the primary purposes of section
5 510(b), therefore, is to prevent disappointed
shareholders, sometimes the victims of corporate fraud,
from recouping their investment in parity with unsecured
creditors.

6 *Id.* This principle applies even when the claimant held stock in a
7 company acquired by the debtor. or even when the claimant has
8 declined to accept shares in a third company that had been
9 tendered to them by debtor following a failed merger. As the
10 Ninth Circuit recently held in *In re Del Biaggio*, 834 F.3d 1003
11 (9th Cir. 2006), a claim for amounts paid for a membership
12 interest in a limited liability company affiliated with the debtor
13 was a claim for damages "arising from" the purchase or sale of
14 securities and was thus subject to subordination under section
15 510(b).

16 Likewise, in *In re Betacom of Phoenix, Inc.*, 240 F.3d 823
17 (9th Cir. 2001), the claimants held shares in a corporation that
18 entered into a merger agreement with the debtor. The agreement
19 called for the claimants to receive stock of the surviving company
20 in exchange for their shares in the acquired company. The merger
21 agreement never closed and claimants never accepted their tendered
22 shares, which remained in escrow. The Ninth Circuit held that
23 even though the claimants never accepted the tendered share
24 resulting from the merger, their claim should be subordinated
25 under section 510(b).

26 In another similar case, *In re Tristar Esperanza Props., LLC*,
27 488 B.R. 394 (9th Cir. BAP 2013), the bankruptcy appellate panel
28 held that section 510(b) subordinates "three types of claims –

1 rescission, damages, and reimbursement/contribution – that all
2 have a nexus with the purchase or sale of a security.” Here,
3 Florek’s claim for damages has a nexus with his purchase of a
4 security. The claim is thus subordinated under section 510(b) as
5 a matter of law. Further briefing or discovery by Moore will not
6 change this result.

7 III. CONCLUSION

8 For the foregoing reasons, the court will sustain the
9 objection to Florek’s claim and deny Moore’s request for further
10 time to respond. Counsel for Debtor should upload an order
11 accordingly, and state that the objection is sustained “for the
12 reasons stated in the memorandum decision entered on [date]”
13 Counsel should also file (on the docket, not appended to the
14 order) a proof of service in accordance with B.L.R. 9021-1(c).

15 *** END OF MEMORANDUM DECISION ***
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Court Service List

Teresa J. Moore
Post Office Box 748
Mountain View, CA 94042